Supreme Court, U.S.
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No. 08-1340

IN THE
Supreme Court of the United States

MATTHEW WIGGENHORN, ET AL.,
Petitioners,

v.

AXA EQUITABLE LIFE INSURANCE COMPANY
FORMERLY KNOWN AS EQUITABLE LIFE ASSURANCE
SOCIETY OF THE UNITED STATES, ET AL.,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

REPLY BRIEF FOR PETITIONERS

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TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES.....ii

ARGUMENT:

I. The Circuits Are Deeply Divided In Assessing When A Complaint Lacking Explicit Allegations Of Misrepresentation Violates SLUSA.....2

A. The Third And Fourth Circuits' Approaches Are Irreconcilable.....2

B. The Circuits Are In Disarray In Their Approaches And Need This Court's Guidance.....5

II. Respondents Offer No Meritorious Reason For Denying the Petition.....10

CONCLUSION.....12

TABLE OF AUTHORITIES

Page

CASES

Anderson v. Merrill Lynch Pierce Fenner & Smith, Inc., 521 F.3d 1278 (10th Cir. 2008) 8,9

Barclay White Skanska, Inc. v. Battelle Mem'l Inst., 262 Fed.Appx. 556 (4th Cir. 2008) 10

Behlen v. Merrill Lynch, 311 F.3d 1087 (11th Cir, 2002) 9

Burks v. Lasker, 441 U.S. 471 (1979) 11

Caterpillar Inc. v. Williams, 482 U.S. 386 (1987) 7

Cochran v. Holder, 564 F.3d 318 (4th Cir. 2009) 10

Dotson v. Pfizer, Inc., 558 F.3d 284 (4th Cir. 2009) 11

Dudek v. Prudential Sec., Inc., 295 F.3d 875 (8th Cir. 2002) 8

Franchise Tax Bd. of Cal. v. Construction Laborers Vacation Trust for S. Cal., 463 U.S. 1 (1983) 6

Green v. Fund Asset Mgmt., L.P., 245 F.3d 214 (3d Cir. 2001) 11

Hanson v. Cerrone & Assoc., Inc., 1993 WL 98777 (4th Cir. 1993) 11

In re Charles Schwab Corp. Sec. Litig.,
257 F.R.D. 534 (N.D. Cal. 2009) 2

In re Mutual Funds Inv. Litig., MDL No.
04-MD-15863, 2009 WL 1725976
(D. Md. June 12, 2009) 3

In re Mut. Fund Market-Timing Litig.,
468 F.3d 439 (7th Cir. 2006) 8

Kircher v. Putnam Funds Trust, 403 F.3d 478
(7th Cir. 2005), *vacated on jurisdictional grounds*, 547 U.S. 633 (2006)..... 7

Kircher v. Putnam Funds Trust,
547 U.S. 633 (2006) 7

LaSala v. Bordier et Cie,
519 F.3d 121 (3d Cir. 2008) 2, 3, 6

Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit, 547 U.S. 71 (2006) 8

Miller v. Nationwide Life Ins. Co.,
391 F.3d 698 (5th Cir. 2004) 9

Rivet v. Regions Bank of Louisiana,
522 U.S. 470 (1998) 5,6

Scott v. Stone,
945 F.2d 398 (4th Cir. 1991) 10

United States v. Almendarez,
1 Fed.Appx. 234 (4th Cir. 2001) 10-11

United States v. Ferguson,
48 F.3d 1217 (4th Cir. 1995) 11

United States v. Uribe-Rios,
558 F.3d 347 (4th Cir. 2009) 10

U.S. Mortgage, Inc. v. Saxton,
494 F.3d 833 (9th Cir. 2007) 9

Xpedior Creditor Trust v. Credit Suisse First Boston (USA) Inc, 341 F. Supp. 2d 258 (S.D.N.Y. 2004) 6

STATUTES AND REGULATIONS

Securities Act of 1933, 15 U.S.C. § 77p(b) 6

Securities Exchange Act of 1934,
15 U.S.C. § 78bb(f)(1)..... 6

Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353,
112 Stat. 3227 ..... *passim*

15 U.S.C. § 80a-49 11

A deep conflict exists among the circuits regarding when SLUSA bars state law claims which do not include explicit allegations of misrepresentations or omissions of material fact. In spite of the Court's request for respondents to file a brief, respondents still make no effort to address the circuit conflict, the widespread confusion among the federal courts, or the appropriateness of this Court's resolution of the conflict on the undisputed factual record presented by this case. Respondents acknowledge "differences in articulation" of the "substantive inquiry" the courts of appeals undertake to assess whether a claim is an attempt to artfully plead around SLUSA; but they attempt to pass off these differences as merely "different verbal formulations" that are not outcome-determinative. Opp. 12-13. Respondents do not discuss what those acknowledged "differences" are or how those "differences" are merely different ways of saying the same thing — and for good reason. The courts of appeals are actually poles apart on this important issue.

Instead of addressing the circuit conflict, respondents focus on the circuit unanimity for the non-controversial principle that a plaintiff may not "artfully plead" around SLUSA. Respondents ignore the fact that the agreement ends there. The circuit tests for determining whether a plaintiff's allegations are an "artful" attempt to dodge SLUSA are in hopeless conflict.

At one end, the Third Circuit has held that deceit must be a "factual predicate" of the claim actually pleaded to trigger SLUSA. The Seventh Circuit has staked out the opposite extreme, holding that a claim need only be susceptible of being recast as a claim of deceit: if the plaintiff's claim "could have" been cast as a deception claim, that is sufficient to trigger SLUSA. The Fourth and

Eighth Circuits' rationales are vague, but both circuits seem to follow the rule that if a plaintiff has previously asserted a deception-based claim, SLUSA bars subsequent claims, even when the plaintiff unconditionally abandons that claim in favor of a claim not predicated on deception.

Respondents' unexplained insistence that these admitted "differences" are not outcome-determinative conflicts is disingenuous. This Court's review is essential to restore uniformity to the circuits' irreconcilably divergent interpretations of the Securities Litigation *Uniform* Standards Act of 1998.

I. The Circuits Are Deeply Divided In Assessing When A Complaint Lacking Explicit Allegations Of Misrepresentation Violates SLUSA.

A. The Third And Fourth Circuits' Approaches Are Irreconcilable.

Respondents' attempt to harmonize the Fourth Circuit's holding with the Third Circuit's decision in *LaSala v. Bordier et Cie*, 519 F.3d 121 (3d Cir. 2008), is entirely unconvincing. Respondents claims that the cases are not in conflict simply because both circuits agree a plaintiff cannot "artfully plead" around SLUSA.[1] No court has disagreed with that general proposition nor do petitioners. The circuit conflict involves the imple-

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[1] Respondents initially attempt to dismiss *LaSala*'s holdings as involving "very different and unique questions" that "bear little resemblance to the SLUSA question presented here." Opp. 11. That claim is meritless. The "factual predicate" discussion in *LaSala*, 519 F.3d at 141, directly addresses the precise SLUSA-pleading question presented here, as at least one court has recognized. *See In re Charles Schwab Corp. Sec. Litig.*, 257 F.R.D. 534, 551 (N.D. Cal. 2009) (relying on *LaSala*'s factual predicate test).

mentation of that general principle, and the circuit approaches are starkly different.

The Third Circuit holds that SLUSA's misrepresentation "ingredient" is present only "when an allegation of misrepresentation in connection with a securities trade, implicit or explicit, operates as a factual predicate to a legal claim." *LaSala*, 519 F.3d at 141. "To be a factual predicate, the fact of a misrepresentation must be one that gives rise to liability." *Id.* When a misrepresentation or omission is a factual predicate of a legal claim, a plaintiff's omission of that allegation is "artful pleading," and SLUSA bars the claim.

By contrast, the Fourth Circuit held that petitioners' claim "that Defendants negligently exposed [petitioners'] investments to the dilution effect of market timing" runs afoul of SLUSA. Pet. App. 5a. The same district judge who dismissed these cases (which are part of a multidistrict proceeding involving numerous other market timing cases), recently vindicated petitioners' position that their claims are negligence claims, not fraud: "Even if plaintiffs are correct that Janus should have implemented [practices] ... and established written policies [to curb market timing], *plaintiffs would only prove a case of negligence or corporate mismanagement — not a fraud claim.*" *In re Mutual Funds Inv. Litig.*, MDL No. 04-MD-15863, at *3 2009 WL 1725976 (D. Md. June 12, 2009) (emphasis added). When petitioners' negligence claims were before the district judge, however, he ruled they were "at bottom" fraud claims. Pet. App. 16a.

Because petitioners' claims are properly viewed as negligence claims, it is unsurprising the Fourth Circuit identified no misrepresentation, explicit or implicit, that was the "factual predicate" of their

negligence claims. In fact, petitioners explicitly alleged that respondents "did ***not*** make an untrue statement, fail to disclose any material fact or use or employ any manipulative or deceptive device or contrivance." Pet. App. 33a, 52a, 98a. Thus, had the Fourth Circuit applied the Third Circuit's "factual predicate" test to petitioners' allegations, the court could not have concluded that SLUSA bars petitioners' negligence claims.

Although the Fourth Circuit offered no rationale consistent with the Third Circuit's approach, respondents attempt to do so. According to respondents, "the essential predicate of petitioners' complaints is that the Companies mispriced certain securities," which respondents say is "functionally indistinguishable from a claim that the Companies misrepresented the true value of the securities." Opp. 13. That, however, distorts both the undisputed facts and petitioners' claims.

It is undisputed that variable annuities are not priced or traded like stocks traded on an exchange. Instead, respondents calculate the price of their variable annuities only once per day after the close of trading at 4:00 p.m. Pet. App. 26a. As a result, when investors place their trade orders throughout the course of the day, they do not know the exact price at which their trades will be executed, because their trade orders are also executed only once per day after the close of trading at 4:00 p.m. Pet. App. 26a. Once the new daily price is calculated, that day's trade orders are then executed.

Petitioners allege that when respondents execute a market timer's purchase order at a negligently calculated price, existing investors are injured at that moment by that act. The market timer's purchase at a bargain price dilutes the in-

vestments of all existing investors. Pet. App. 31a-32a. Neither respondents' negligent calculation of the price nor petitioners' economic injury depends on any representation (or *mis*representation) of the price to anyone. It is undisputed that both respondents' negligent calculation of the price and petitioners' injury occur hours before the new daily price is ever published or represented to anyone.[2] Because no representation plays any role in petitioners' injury, a misrepresentation cannot be a factual predicate of petitioners' claims for that injury. Respondents' attempt to square the Fourth Circuit's holding with *LaSala* therefore fails.

B. The Circuits Are In Disarray In Their Approaches And Need This Court's Guidance.

Respondents portray the circuits as being in harmony on "the SLUSA-pleading question." Opp. 6-7. As noted, however, the circuits agree only at the most general level that a plaintiff may not "artfully plead" around SLUSA. The circuits are deeply divided regarding how to determine when a complaint lacking explicit allegations of misrepresentation violates SLUSA. That is the actual "SLUSA-pleading question" these cases present — and which respondents never discuss.

The artful pleading doctrine was developed long before the enactment of SLUSA in the context of federal question jurisdiction. *See Rivet v. Regions Bank of Louisiana*, 522 U.S. 470, 474-75 (1998) (discussing evolution of artful pleading doctrine).

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[2] In addition, when the price is eventually published hours later, it is not a misrepresentation. It is the true per-unit price respondents calculated, and it is the actual per-unit price at which respondents executed all trade orders.

Under that doctrine, "a plaintiff may not defeat removal [jurisdiction] by omitting to plead necessary federal questions." *Id.* at 475 (quoting *Franchise Tax Bd. of Cal. v. Construction Laborers Vacation Trust for S. Cal.*, 463 U.S. 1, 14 (1983)).

SLUSA prohibits a plaintiff in a state-law class action from "alleging an untrue statement or omission of a material fact in connection with the purchase or sale of a covered security." 15 U.S.C. § 77p(b); *accord id.* § 78bb(f)(1). Thus, applying the artful pleading doctrine in the SLUSA context, a plaintiff may not defeat SLUSA by omitting to allege an untrue statement or omission necessary to the properly pleaded state law claim. Conversely, if an untrue statement, misrepresentation or omission is *not* necessary to the properly pleaded state law claim, SLUSA does not bar the claim. Such a necessary allegation of an untrue statement, misrepresentation or omission is what the Third Circuit refers to as a "factual predicate." *LaSala v. Bordier et Cie*, 519 F.3d 121, 141 (3d Cir. 2008). *See Xpedior Creditor Trust v. Credit Suisse First Boston (USA) Inc.*, 341 F.Supp.2d 258, 266 (S.D.N.Y. 2004) (applying a similar "necessary component" test).

The Third Circuit's "factual predicate" test is thus a faithful application of the artful pleading doctrine in the SLUSA context. It is not a "mechanistic review of the 'party's pleadings' that stops at the face of the complaint and ignores any fair or realistic reading of the claims," and contrary to respondents' assertion, petitioners do not advocate such a "mechanistic" approach. Opp. 13. However, the review SLUSA requires must at least *begin with* a review of a complaint's allegations, which the Fourth, Seventh and Eighth Circuits' approaches do not.

As explained in the petition, the Seventh Circuit has taken the view that allegations not found in a complaint, but instead hypothesized by a court, are sufficient to trigger SLUSA. *Kircher v. Putnam Funds Trust*, 403 F.3d 478, 484 (7th Cir. 2005), *vacated on jurisdictional grounds*, 547 U.S. 633 (2006). ("Suppose the funds stated in their prospectuses that they took actions to prevent arbitrageurs from" market timing; "[t[hat statement, if false (and known to be so), could support [an SEC] enforcement action"). In the Seventh Circuit's view, simply because the plaintiffs "could have" — with the addition of the hypothetical allegations — "brought [their claims] directly under Rule 10b-5 in federal court," they must necessarily be viewed as fraud claims barred by SLUSA. *Id.*

The Seventh Circuit's approach is not only at odds with the Third Circuit's "factual predicate" test, it is also inconsistent with SLUSA which bars claims on the basis of what a plaintiff is actually "alleging," not on the basis of what a plaintiff "could have" alleged. Furthermore, the *Kircher* approach flatly contradicts this Court's precedents: "The 'artful pleading' doctrine cannot be invoked" "on the basis of facts not alleged in the complaint." *Caterpillar Inc. v. Williams*, 482 U.S. 386, 397 (1987).

Respondents do not seriously attempt to defend the Seventh Circuit's reliance on hypothetical allegations. Instead, respondents dismiss *Kircher* as "irrelevant to any claimed circuit conflict because this Court vacated the decision for lack of jurisdiction." Opp. 10 n.5 (citing *Kircher v. Putnam Funds Trust*, 547 U.S. 633, 648 (2006)). Subsequent to this Court's decision in *Kircher*, however, the Seventh Circuit reaffirmed its SLUSA analysis in that vacated decision, explaining that the Supreme Court "agreed with" its "substantive ap-

proach" in *Kircher* but "concluded that we lacked appellate jurisdiction and v. ated our judgment accordingly." *In re Mut. Fund Market-Timing Litig.*, 468 F.3d 439, 441 (7th Cir. 2006) (citing *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, 547 U.S. 71 (2006)). The Seventh Circuit's *Kircher* decision thus continues to be very relevant to the circuit conflict.

Respondents do not attempt to reconcile the Eighth Circuit's decision in *Dudek v. Prudential Sec., Inc.*, 295 F.3d 875 (8th Cir. 2002), with the Third Circuit's "factual predicate" test, nor could they credibly do so. As explained in the petition, the plaintiffs sued Prudential for breaching their fiduciary duty by charging excessive fees, and their complaint lacked any explicit allegations of misrepresentation or non-disclosure, although the plaintiffs had previously made such allegations in an earlier lawsuit. Pet. 20 (quoting *Dudek*). The Eighth Circuit did not attempt to explain how the claims in the complaint before it were necessarily predicated on misrepresentations or omissions. 295 F.3d at 879-80. As the Fourth Circuit (and the district court) did here, the Eighth Circuit just conclusorily declared that the "substance" and "essence" of the unquoted complaint amounted to "artfully concealed" allegations of misrepresentation or omission. *Id.*

Respondents cite four other cases from the Fifth, Ninth, Tenth and Eleventh Circuits ("ignored by the petition" (Opp. 10)), once again for the general proposition that SLUSA precludes claims of misrepresentation or omission "regardless of how artfully or cleverly plaintiffs attempt to plead them." *Anderson v. Merrill Lynch Pierce Fenner & Smith, Inc.*, 521 F.3d 1278, 1286 (10th Cir. 2008). In three of those cases, the courts had no occasion to apply the artful pleading doctrine,

however, because each involved explicit allegations of misrepresentation or omission; the plaintiffs had not omitted such allegations in an attempt to artfully plead around SLUSA.[3] Consequently, those three cases are irrelevant to the circuit conflict here.

The fourth case also sheds little light on this issue. In *Behlen v. Merrill Lynch*, 311 F.3d 1087, 1089, 1094 (11th Cir. 2002), the plaintiff explicitly alleged misrepresentations and omissions, allegations he later abandoned. It may be that the Eleventh Circuit's decision in *Behlen* is one more instance of a circuit court unduly expanding SLUSA's scope, like the Eighth Circuit did in *Dudek* and the Fourth Circuit has done here. The Eleventh Circuit strongly suggests (as does *Dudek*) that allegations of *any* kind of "misconduct" can trigger SLUSA, *id.* at 1096, even though the only "misconduct" SLUSA addresses is *deceptive* misconduct.

What distinguishes *Behlen*, however, is that it appears the plaintiff merely deleted his misrepresentation claim and deleted other explicit allegations of fraud and omission while simultaneously retaining the exact same underlying theory of the case, which was based on deception. If that was indeed what happened, then *Behlen* is a text-book example of genuine "artful pleading." If anything,

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[3] *Anderson*, 521 F.3d at 1283 ("Plaintiffs made several allegations in their Complaint regarding 'misrepresentation[s] or omission[s] of a material fact'"); *U.S. Mortgage, Inc. v. Saxton*, 494 F.3d 833, 840 (9th Cir. 2007) (amended complaint alleges that defendant "made material misrepresentations concerning the financial status of the company"); *Miller v. Nationwide Life Ins. Co.*, 391 F.3d 698, 702 (5th Cir. 2004) (complaint "alleges 'untrue statement[s]' and 'omission[s]'").

the ambiguity of *Behlen* — resulting from the Eleventh Circuit's failure to carefully parse the plaintiff's allegations like the Third Circuit did in *LaSala* — supports granting the petition here.

II. Respondents Offer No Meritorious Reason For Denying the Petition.

To shore up their claim that there is no circuit split, respondents resort to analysis-by-label. First, respondents describe the Fourth Circuit's analysis as "record-bound," but they fail to explain that assertion or how a decision by this Court would resolve only this case and no others. This Court's decision on the proper mode of analyzing a complaint under SLUSA would be of immense benefit in the numerous market timing cases pending below in the MDL proceeding from which these cases came. Additionally, the conflicting circuit decisions demonstrate that the issue is an oft-recurring one. Respondents offer no reason to doubt that the impact of this Court's decision extends far beyond the present case, and their claim that the Fourth Circuit's analysis is "record-bound" is not credible.

Respondents also emphasize that the Fourth Circuit's decision is "unpublished," suggesting that this diminishes the importance of the decision. A cursory review of Fourth Circuit case law, however, reveals that the Fourth Circuit cites and relies upon its own unpublished opinions regularly.[4] Thus, the decision's "unpublished" designa-

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[4] *See, e.g.*, *Cochran v. Holder*, 564 F.3d 318, 321 (4th Cir. 2009) (citing *Scott v. Stone*, 945 F.2d 398 (4th Cir. 1991) (unpublished)); *Wahi v. Charleston Area Med. Center, Inc.*, 562 F.3d 599, 617 (4th Cir. 2009) (citing *Barclay White Skanska, Inc. v. Battelle Mem'l Inst.*, 262 Fed.Appx. 556 (4th Cir. 2008)); *United States v. Uribe-Rios*, 558 F.3d 347, 352, 358 (4th Cir. 2009) (citing *United States v. Almendarez*,

tion does not detract from the need for this Court's review.

Finally, in the closing paragraph of their brief, respondents contend the Court should deny certiorari because petitioners will ultimately lose on other grounds. Specifically, respondents contend that the Investment Company Act of 1940 "preempts the field" of law governing plaintiffs' claims, an issue which *neither* of the courts below addressed. Opp. 14. Even were there some colorable merit to respondents' "field preemption" argument, that would be no ground for denying certiorari on the question presented under a wholly unrelated statute. The argument, however, is utterly meritless.

The ICA itself provides: "nor shall anything in this subchapter affect the jurisdiction of ... any State or political subdivision of any State, over any person, security, or transaction, insofar as such jurisdiction does not conflict with any provision of this subchapter or of any rule, regulation, or order hereunder." 15 U.S.C § 80a-49. This Court has also held that the ICA does "not require that federal law displace state laws ... unless the state laws permit action prohibited by the Act[], or unless 'their application would be inconsistent with the federal policy ....'" *Burks v. Lasker*, 441 U.S. 471, 479 (1979). *See also Green v. Fund Asset Mgmt., L.P.*, 245 F.3d 214, 225-26 (3d Cir. 2001) (holding that ICA did not preempt state law claims because ICA was intended to supplement state law, not displace it). Respondents' "field pre-

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1 Fed.Appx. 234 (4th Cir. 2001) and *United States v. Ferguson*, 48 F.3d 1217 (4th Cir. 1995) (unpublished)); *Dotson v. Pfizer, Inc.*, 558 F.3d 284, 302 n.9 (4th Cir. 2009) (citing *Hanson v. Cerrone & Assoc., Inc.*, 1993 WL 98777 (4th Cir. 1993)).

emption" argument is no basis for denying certiorari.

CONCLUSION

For the foregoing reasons and those stated in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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